



TRICOM

20 February 2006

REX | \$1.15

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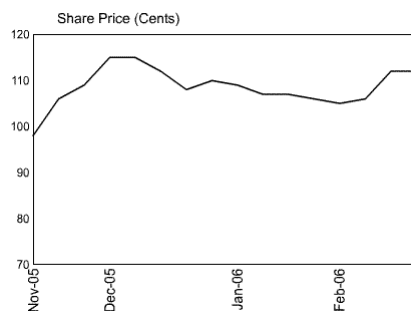
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Fully diluted shares
on issue | 115.0M
Market cap | A\$132.3M

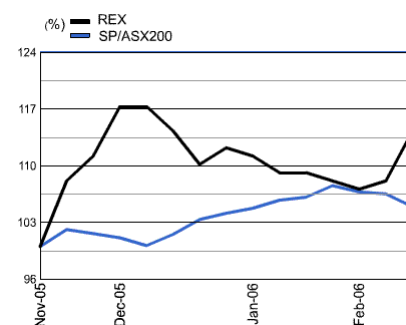
Performance & Valuation

Last Price | \$1.15
52 wk hi/low | \$1.18 / \$0.95
12 month price target³ | \$1.68
Valuation | \$1.54
Valuation methodology | DCF

Share price performance



REX versus SP/ASX200



Regional Express Holdings Ltd|REX

1H06 result - up, up and away!

Key points

- REX reported a very solid 1H06 result, which, it was noted exceeded budget expectations.
- The company reported revenue of \$77.9M and NPAT of \$9.3M (AIFRS and with notional tax expense of \$3.9M).
- The pre-tax figure, given REX is unlikely to pay tax for FY06, was \$13.2M.
- Generally, the seasonal sway in earnings is 55% 1H, 45% 2H. However, there are a number of factors that add to the momentum in the current six months.
- The company was upbeat regarding its performance across all key areas and noted that recent trading had been robust.
- No dividend was declared (and none forecast, as per the Prospectus).
- The potential threat to South Australian destinations following the withdrawal of Airlines of South Australia from the State and replacement by QantasLink, has not eventuated. There was some initial price tension which quickly dissipated.

Comment

We have not altered our earnings forecasts for FY06 or FY07, which we note include Air Link and thus differ modestly from the Prospectus figures. However, the interim result was stronger than we had anticipated in a number of areas, notably operating cashflow which came in a tad below \$14M. Moreover, the shift away from QantasLink for management of the travel arrangements for NSW Government employees is only now starting to gain some traction and that impact could be sizeable.

Pel-Air was up substantially in 1H06 and added to the fact that fuel costs are so far on average below the Prospectus forecast by almost US\$10bbl, we believe REX will comfortably meet it IPO forecasts.

Investment View

With greater balance sheet transparency, we have made adjustments to our cash levels. Accordingly, both our valuation and 12 month price target increase to \$1.54 and \$1.68 from \$1.40 and \$1.56 respectively.

No matter how we look at it, and even conceding the fact that REX is an airline, the shares currently offer extremely good value (6x cashflow FY06 and 4.6x FY07).

Earnings Summary

Y/E Jun	2005A	2006F	2007F
Revenue - A\$M	137.1	150.6	163.1
EBITDA - A\$M	16.2	24.0	29.6
NPAT (reported) A\$M	13.5	19.6	20.0
NPAT (normalised) A\$M ¹	13.5	19.6	20.0
EPS (diluted) - cents ²	16.9	18.4	17.4
EPS (diluted) - % chg	n/a	9.3	(5.6)
PER (diluted) - x ²	6.8	6.2	6.6
DPS - cents	0.0	0.0	4.5
Dividend Yield - %	0.0	0.0	3.9
Franking - %	0	0	0

Notes:

1. Normalised earnings is pre goodwill, amortization and after adding back non-recurring items.
2. Based on normalized earnings.
3. Price target is calculated by moving current valuation one year forward.

Final results analysis & outlook

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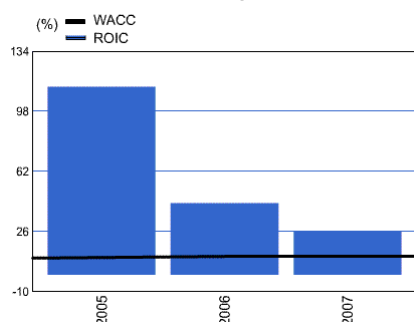
Valuation

Methodology: DCF¹

Key assumptions

Beta	1.3
WACC %	11.2
Forecast period years	10.0
Risk premium %	5.5
PV cash flows \$M	157.6
less net debt/(add cash) \$M	(20.0)
add equity adjustments ²	0.0
Total	177.6
Fully diluted shares on issue M ²	115.0
Value per share \$	1.54

Return on invested capital



Ratio analysis

Year end Jun	05A	06F	07F
Revenue growth %	0.0	9.8	8.3
EBITDA growth %	n/a	48.1	23.5
EBITDA margin %	11.8	15.9	18.2
EBIT margin %	9.0	13.0	14.6
Tax rate %	0.0	8.3	30.0
ROA %	31.0	24.7	23.8
ROE %	96.8	34.9	23.4
Net debt/equity %	0.5	(1.5)	(21.0)
Net interest cover x	17.7	67.4	n/a
Capex to deprec'n %	397.4	303.5	98.5
NTA per share \$	0.23	0.66	0.81

Multiple analysis

Year end Jun	05A	06F	07F
Market cap M	132		
Net debt (cash) \$M	(20.0)		
Options \$M	0.0		
Enterprise value \$M	112		
EV/EBITDA x	6.9	4.7	3.8
EPS c	16.9	18.4	17.4
P/E x	6.8	6.2	6.6
Cashflow / Share c	(7.4)	13.1	23.1
Price / NTA x	4.9	1.7	1.4

Shares outstanding

Year end Jun	05A	06F	07F
Basic M	80.0	115.0	115.0
Other M	0.0	0.0	0.0
Fully diluted M	80.0	115.0	115.0

Notes:

1. Discounted cash flow. 2. Equity adjustments and shares on issue include all notes and options on issue (if in the money or deemed appropriate).

Year end Jun	2005A	2006F	2007F
Profit & Loss Summary A\$M			
Operating revenue	137.1	150.6	163.1
Invest & other income	0.0	0.0	0.0
EBITDA	16.2	24.0	29.6
Depreciation/Amort	(3.8)	(4.4)	(4.4)
EBIT	12.4	19.6	25.3
Net Interest	(0.7)	0.0	1.8
Pre-tax profit	11.7	19.7	27.0
Tax expense	0.0	(1.5)	(8.1)
Minorities/Assoc./Prefs	1.8	1.8	2.9
NPAT	13.5	20.0	21.8
Non recurring items	0.0	0.0	0.0
Reported profit	13.5	20.0	21.8
add goodwill/non recurring	0.0	0.0	0.0
Adjusted profit	13.5	20.0	21.8
Cashflow Summary A\$M			
EBITDA	16.2	24.0	29.6
Working capital changes	0.0	(2.5)	(0.1)
Interest and tax	(0.6)	1.0	(2.1)
Other operating items	(21.5)	0.4	0.0
Operating cashflow	(5.9)	22.9	27.5
Required capex	(15.1)	(13.7)	(5.7)
Maintainable cashflow	(21.0)	9.1	21.8
Dividends/Other	0.0	0.0	(2.9)
Acq/Disp	6.4	(13.2)	(5.0)
Other investing items	4.2	(2.8)	0.0
Free cashflow	(10.4)	(6.9)	13.9
Equity	0.0	35.0	0.0
Debt inc/(red'n)	4.6	(8.3)	(13.9)
Balance Sheet A\$M			
Cash & deposits	4.5	26.1	40.0
Inventories	3.0	3.4	3.8
Trade debtors	7.3	6.6	6.6
Other curr assets	4.5	1.3	1.3
Total current assets	19.3	37.4	51.7
Prop., plant & equip.	24.5	34.9	41.3
Non-curr intangibles	0.0	0.7	0.7
Non-curr investments	1.9	13.9	16.8
Other non-curr assets	4.6	12.4	12.4
Total assets	50.3	99.4	123.0
Trade creditors	12.4	15.7	16.0
Curr borrowings	0.5	0.5	0.5
Other curr liabilities	13.5	0.9	5.1
Total current liab.	26.4	17.0	21.6
Borrowings	4.1	0.0	0.0
Other non-curr liabilities	1.2	1.2	1.2
Total liabilities	31.7	18.2	22.8
Minorities/Convertibles	0.0	0.0	0.0
Shareholders equity	18.6	81.2	100.2

Year end Jun	2005A	2006F	2007F
Divisional Summary A\$M			
Revenue			
REX	137.1	146.6	155.9
Air Link	0.0	4.0	7.2
EBITDA			
REX	16.2	23.8	28.2
Air Link	0.0	0.2	1.5
Margin %			
REX	11.8	16.2	18.1
Air Link	0.0	5.0	20.3

Result detail

Highlights

Rex produced a very solid 1H06 result, its first as a publicly listed company:

Six months to 31 Dec 05	1H06 (\$M)	1H05 (\$M)	% change
Revenue*	75.0	64.5	16%
EBITDAR	17.4	8.5	105%
Share of associate	1.0	-	
NPAT	9.3	2.7	244%
EPS	10.0c	5.0c	100%

Source: REX

Notes: * including fuel levy recovery

The highlights of the result were:

Revenue and associates

Revenue

- Passenger revenue contributed 99%, or \$74.1M of total revenue.
- There was an 11% increase in passenger numbers, from 528K in 1H05 to 584K in 1H06, with load factors increasing to 66.3% from 65.6% pcp.
- Fares rose 5%, reflecting the increase in the fuel surcharge. However, ignoring the surcharge, average fares in fact declined by 5%.
- REX reported that it is seeing some traction in NSW public service traffic, following the shift from QantasLink in December 2005. We see this as a major contributing factor to earnings in 2H06 and beyond.
- There was an additional \$0.8M in revenue (that fed directly through to the bottom line) from a downward adjustment to a superannuation liability in relation to the divestment of Hazelton Air Services. This was not a cash item.

Air Link

- The contribution made by Air Link (100% owned) purchased on 30 November 2005 was \$30K. Had the company been acquired as at 1 July 2006, it would have contributed \$115K to earnings.
- It was noted that Air Link is enjoying huge synergistic benefits from its marriage with Rex, with fuel purchasing savings of 12% and substantial cost benefits in ground handling (particularly at Sydney airport where facilities for Air Link and Rex have been merged).
- The concerns that Air Link held for a possible loss in market share with the demise of its partnership agreement with QantasLink, have proven unfounded and the company has enjoyed increased market penetration through its marriage to REX.

Pel-Air

The 50% owned associate, Pel-Air, acquired 1 July 2005, delivered a 41% lift in its 1H06 results (\$1M contribution to REX's bottom line). This result was 7% better than budget and the momentum was expected to be continued into 2H06.

Costs

- Improved productivity resulted in cost per available seat kilometre (ASK) falling 5% from 20.2 cents to 19.1 cents. Based on REX data, REX operated on (by far) the greatest PBT/Revenue margin (17% 1H06) than any of its peers.
- Fuel costs remain a primary expense (second only to staff costs \$21.4M) at \$12.9M and up 30% pcp. REX does not hedge its fuel costs and we understand it paid an equivalent of just above US\$70bbl (c/f forecast of US\$79bbl for FY06) for fuel in 1H06.
- Given 11% capacity growth, significantly higher fuel costs and staff up by 11 more on the payroll, costs were controlled, rising by a modest 6%. If adjusted for the 30% increase in fuel costs, expenditure in fact fell 1% pcp.
- Selling costs fell 21%, due to recovery of credit card expenses from passengers and reduction in commissions to agents.
- The purchase of two previously leased aircraft, resulted in a 6% drop in operating lease rental costs. The fleet now comprises 29 aircraft.

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As at the time of writing this report, the author holds shares in Regional Express Limited (REX), which were acquired as part of the REX IPO, in November 2005.

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